

Internal Revenue Service

Number: **201108018**

Release Date: 2/25/2011

Index Number: 851.02-00

Department of the Treasury

Washington, DC 20224

Third Party Communication: None

Date of Communication: Not Applicable

Person To Contact:

, ID No.

Telephone Number:

Refer Reply To:

CC:FIP:B02

PLR-132486-10

Date:

November 15, 2010

Legend:

Taxpayer =

Trust =

State =

Date 1 =

Total Return Index =

Excess Return Index =

Total Return Sub Index =

Excess Return Sub Index =

a =

b =

c =

d =

e =

f =

g =

Country =

Type A Company =

Dear _____ :

This responds to your request dated August 4, 2010, submitted by your authorized representative on behalf of Taxpayer. Taxpayer requests that the Internal Revenue Service rule that: (1) income and gain arising from the commodity-linked notes described in this letter will constitute qualifying income to Taxpayer under section 851(b)(2) of the Internal Revenue Code of 1986, as amended ("the Code"), and (2) income derived by Taxpayer from its investment in controlled foreign corporation subsidiaries (CFCs) will constitute qualifying income to Taxpayer under section 851(b)(2) of the Code.

Facts:

Taxpayer is a series of Trust. Trust is a State statutory trust registered as an open-end series investment company under the Investment Company Act of 1940, 15 U.S.C. 80a-1 et seq., as amended (the "1940 Act"). Taxpayer intends to elect and qualify as a regulated investment company ("RIC") under Subchapter M of the Code. Taxpayer uses an accrual method of accounting and a fiscal year ending on Date 1.

Commodity-Linked Notes:

Taxpayer intends to invest in commodity-linked notes having the terms and conditions of the following four notes (the Notes):

Note A:

The first note will be issued at a par value of \$a. Its payout formula will be determined with reference to the value of a Total Return Index. The term of Note A will be twenty-four months. A Fund, as holder of Note A, will have the right to put Note A to the issuer at the calculated redemption price based on the closing Total Return Index value as of the end of the next day after notification to the issuer. In addition, if the Total Return Index value falls b% from the value at the time Note A is acquired, Note A will "knock-out" and automatically redeem based on a redemption price calculated using the closing Total Return Index value of the next day.

The repayment obligation upon early redemption, automatic redemption, or maturity is calculated under a formula that provides for repayment of the face amount of Note A increased or decreased by an amount equal to the face amount of Note A multiplied by a leverage factor of c multiplied by the percentage of the increase or decrease of the beginning Total Return Index value level compared to the ending Total Return Index value level for the applicable period. To this amount is added an amount that reflects interest on Note A at a coupon rate of d. From this amount is subtracted an

annual fee amount of e basis points of the notional value (leveraged face amount) of Note A.

Note B:

Note B will be issued at a par value of \$a. Its payout formula will be determined with reference to the value of a Total Return Subindex. The term of Note B will be thirteen months. A Fund, as holder of Note B, will have the right to put Note B to the issuer at the calculated redemption price based on the closing Total Return Subindex value as of the end of the next day after notification to the issuer. In addition, if the Total Return Subindex value falls e% from the value at the time Note B is acquired, Note B will “knock-out” and automatically redeem based on a redemption price calculated using the closing Total Return Subindex value of the next day.

The repayment obligation upon early redemption, automatic redemption, or maturity is calculated under a formula that provides for repayment of the face amount of Note B increased or decreased by an amount equal to the face amount of Note B multiplied by a leverage factor of f multiplied by the percentage of the increase or decrease of the beginning Total Return Subindex value level compared to the ending Total Return Subindex value level for the applicable period. To this amount is added an amount that reflects interest on Note B at a coupon rate of d. From this amount is subtracted an annual fee amount of g basis points of the notional value (leveraged face amount) of Note B.

Note C:

Note C will be issued at a par value of \$a. Its payout formula will be determined with reference to the value of an Excess Return Index. The term of Note C will be thirteen months. A Fund, as holder of Note C, will have the right to put Note C to the issuer at the calculated redemption price based on the closing Excess Return Index value as of the end of the next day after notification to the issuer. In addition, if the Excess Return Index value falls e% from the value at the time Note C is acquired, Note C will “knock-out” and automatically redeem based on a redemption price calculated using the closing Excess Return Index value on the next day.

The repayment obligation upon early redemption, automatic redemption, or maturity is calculated under a formula that provides for the repayment of the face amount of Note C increased or decreased by an amount equal to the face amount of Note C multiplied by a leverage factor of f multiplied by the percentage of the increase or decrease of the beginning Excess Return Index value level compared to the ending Excess Return Index value level for the applicable period. To this amount is added an amount that reflects interest on Note C at the coupon rate of d. From this amount is subtracted an annual fee amount of e basis points of the notional value (leveraged face amount) of Note C.

Note D:

Note D will be issued at a par value of \$a. Its payout formula will be determined with reference to the value of an Excess Return Subindex. The term of the Note will be twenty-four months. A Fund, as holder of Note D, will have the right to put Note D to the issuer at the calculated redemption price based on the closing Excess Return Subindex value as of the end of the next day after notification to the issuer. In addition, if the Excess Return Subindex value falls e% from the value at the time Note D is acquired, Note D will “knock-out” and automatically redeem based on a redemption price calculated using the closing Excess Return Subindex value calculated on the next day.

The repayment obligation upon early redemption, automatic redemption, or maturity is calculated under a formula that provides for repayment of the face amount of Note D increased or decreased by an amount equal to the face amount of Note D multiplied by a leverage factor of f multiplied by the percentage of the increase or decrease of the beginning Excess Return Subindex value compared to the ending Excess Return Subindex value level for the applicable period. To this amount is added an amount that reflects interest on Note D at the coupon rate of d. From this amount is subtracted an annual fee amount of g basis points of the notional value (leveraged face amount) of Note D.

Taxpayer makes the following representations with respect to these four Notes:

- (1) The issuer of the Notes has received or will receive payment in full of the purchase price of the Notes substantially contemporaneously with the delivery of the Notes;
- (2) Taxpayer, while holding the Notes, will not be required to make any payment to the issuer of the Notes in addition to the purchase price paid for the Notes, whether as margin, settlement payment, or otherwise, during the life of the Notes or at maturity;
- (3) The issuer of the Notes is not subject by the terms of the instrument to mark-to-market margining requirements of the Commodities Exchange Act, 7 U.S.C. 2, as amended (CEA); and
- (4) The Notes are not marketed as a contract of sale of a commodity for future delivery (or option on such a contract) subject to the CEA.

Controlled Foreign Corporation

Taxpayer intends to form two wholly-owned subsidiaries (Subsidiary A and Subsidiary B) each incorporated as a Type A Company under the laws of Country. Under the laws of Country, a Type A Company provides limited liability for all holders of shares. A shareholder's liability is limited to the amount, if any, unpaid with respect to the shares acquired by the shareholder. Subsidiary A and Subsidiary B intend to file

elections on Form 8832, Entity Classification Election, to ensure that they will be treated as corporations for federal income tax purposes.

Taxpayer represents that, although neither Subsidiary A nor Subsidiary B will be registered as an investment company under the 1940 Act, each Subsidiary will comply with the requirements of section 18(f) of the 1940 Act, Investment Company Act Release No. 10666, and related SEC guidance pertaining to asset coverage with respect to transactions in commodity swaps, commodity futures and other transactions in derivatives.

Taxpayer will invest a portion of its assets in each Subsidiary, subject to the limitations set forth in § 851(b)(3) of the Code. Subsidiary A is expected to invest in futures and/or swaps on commodities associated with the energy sector such as crude oil, heating oil, natural gas and unleaded gas. Subsidiary A will also invest in futures and/or swaps on commodities associated with livestock such as lean hogs and live cattle.

Subsidiary B will attempt to gain exposure to grains such as wheat, corn and soybeans; industrial metals such as high grade copper; precious metals such as gold and silver; and soft commodities such as cocoa, coffee, cotton and sugar. Such exposure will be gained using futures and/or swaps.

Subsidiary A and Subsidiary B will be wholly-owned by Taxpayer, and both are thus expected to be classified as CFCs, as defined in § 957 of the Code. Taxpayer will include its “subpart F” income attributable to each Subsidiary under the rules in the Code applicable to CFCs.

Law and Analysis

Section 851(b)(2) of the Code provides that a corporation shall not be considered a RIC for any taxable year unless it meets an income test (the “qualifying income requirement”). Under this test, at least 90 percent of its gross income must be derived from certain enumerated sources. A corporation that is a partner in a partnership (other than a qualified publicly traded partnership) must look through such partnership for purposes of meeting the qualifying income requirement. Section 851(b)(2) defines qualifying income, in relevant part, as —

dividends, interest, payments with respect to securities loans (as defined in section 512(a)(5)), and gains from the sale or other disposition of stock or securities (as defined in section 2(a)(36) of the 1940 Act) or foreign currencies, or other income (including but not limited to gains from options, futures or forward contracts) derived with respect to [the RIC's] business of investing in such stock, securities, or currencies. . . .

Section 2(a)(36) of the 1940 Act defines the term "security" as —

any note, stock, treasury stock, security future, bond, debenture, evidence of indebtedness, certificate of interest or participation in any profit-sharing agreement, collateral-trust certificate, preorganization certificate or subscription, transferable share, investment contract, voting-trust certificate, certificate of deposit for a security, fractional undivided interest in oil, gas, or other mineral rights, any put, call, straddle, option, or privilege on any security (including a certificate of deposit) or on any group or index of securities (including any interest therein or based on the value thereof), or any put, call, straddle, option, or privilege entered into on a national securities exchange relating to foreign currency, or, in general, any interest or instrument commonly known as a "security", or any certificate of interest or participation in, temporary or interim certificate for, receipt for, guarantee of, or warrant or right to subscribe to or purchase, any of the foregoing.

Section 2(f)(1) of the CEA provides that the CEA is not applicable to a hybrid instrument that is predominantly a security. Section 2(f)(2) of the CEA provides that a hybrid instrument shall be considered to be predominantly a security if —

(A) the issuer of the hybrid instrument receives payment in full of the purchase price of the hybrid instrument, substantially contemporaneously with the delivery of the hybrid instrument;

(B) the purchaser or holder of the hybrid instrument is not required to make any payment to the issuer in addition to the purchase price paid under subparagraph (A), whether as margin, settlement payment, or otherwise, during the life of the hybrid instrument or at maturity;

(C) the issuer of the hybrid instrument is not subject by the terms of the instrument to mark-to-market margining requirements; and

(D) the hybrid instrument is not marketed as a contract of sale of a commodity for future delivery (or option on such a contract) subject to the CEA.

Section 2(f)(3) of the CEA provides, in part, that for purposes of section 2(f)(2)(C) of the CEA, mark-to-market margining requirements do not include the obligation of an issuer of a secured debt instrument to increase the amount of collateral held in pledge for the benefit of the purchaser of the secured debt instrument to secure the repayment obligations of the issuer under the secured debt instrument.

In addition, the flush language of section 851(b) of the Code provides that, for purposes of section 851(b)(2), there shall be treated as dividends amounts included in gross income under section 951(a)(1)(A)(i) or 1293(a) for the taxable year to the extent

that, under section 959(a)(1) or 1293(c) (as the case may be), there is a distribution out of the earnings and profits of the taxable year which are attributable to the amounts so included.

Section 957 of the Code defines a CFC as any foreign corporation in which more than 50 percent of (1) the total combined voting power of all classes of stock entitled to vote, or (2) the total value of the stock is owned by United States shareholders on any day during the corporation's taxable year. A United States shareholder is defined in section 951(b) as a United States person who owns 10 percent or more of the total combined voting power of all classes of voting stock of a foreign corporation. Taxpayer represents that 100 percent of the voting power of the stock of each Subsidiary will be owned by Taxpayer and that Taxpayer is a United States person. Taxpayer therefore represents that each Subsidiary will qualify as a CFC under these provisions.

Section 951(a)(1) of the Code provides that, if a foreign corporation is a CFC for an uninterrupted period of 30 days or more during any taxable year, every person who is a United States shareholder of this corporation and who owns stock in this corporation on the last day of the taxable year in which the corporation is a CFC shall include in gross income the shareholder's pro rata share of the CFC's subpart F income for the taxable year.

Section 952(a)(2) of the Code defines subpart F income to include foreign base company income determined under section 954. Under section 954(a)(1), foreign base company income includes foreign personal holding company income determined under section 954(c). Under section 954(c)(1), foreign personal holding company income includes (among other things): dividends, interest, royalties, rents, and annuities; gains in excess of losses from transactions in commodities (including futures, forward, and similar transactions but excluding certain hedging transactions and certain active business gains and losses); and, subject to certain exceptions, net income from notional principal contracts.

Subsidiary A and Subsidiary B's investments may generate foreign personal holding company income under section 954(c), which is subpart F income. Taxpayer will therefore include in income its pro rata share of Subsidiary A and Subsidiary B's subpart F income for the taxable year in accordance with section 951.

Conclusion

Based on the facts as represented, we rule that income and gain arising from the Notes constitutes qualifying income to Taxpayer under section 851(b)(2) of the Code. We further rule that subpart F income of Subsidiary A and Subsidiary B attributable to Taxpayer is income derived with respect to Taxpayer's businesses of investing in the stock of Subsidiary A and Subsidiary B and thus constitutes qualifying income to Taxpayer under section 851(b)(2).

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter. In particular, no opinion is expressed with regard to whether Taxpayer qualifies as a RIC under subchapter M of the Code.

This ruling is directed only to the taxpayer requesting it, and is limited to the facts as represented by the taxpayer. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representatives.

Sincerely,

Thomas M. Preston

Thomas M. Preston

Senior Counsel, Branch 2

Office of Associate Chief Counsel

(Financial Institutions & Products)